Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matters of

Winstar Communications LLC	)	
Emergency Petition for Declaratory Ruling	)	
Regarding ILEC Obligations to Continue	)	
Providing Service	)	
	)	WC Docket No. 02-80
Verizon Petition for Declaratory Ruling	)	
Regarding CLEC Obligations to Cure	)	
Assigned Indebtedness	)	

COMMENTS OF
Z-TEL COMMUNICATIONS, INC.

A fundamental principle of bankruptcy law is that bankruptcy law respects all rights that exist outside of bankruptcy. This key principle, known as the *Buntner* principle, holds that "there is no reason why [the legal] interests [of a bankrupt estate] should be analyzed differently simply because an interested party is involved in a bankruptcy proceeding." *Buntner v. United States*, 440 U.S. 48, 55 (1979). Verizon's Petition for a Declaratory Ruling asks the Commission to contravene this principle by changing its substantive policies in circumstances where a CLEC is in bankruptcy. That Petition would reward incumbent LECs for abusing their market position and would be bad public policy.

Z-Tel Communications, Inc. ("Z-Tel") is a Tampa, Florida-based integrated communications provider that offers local, long-distance and enhanced services to over a quarter million mass-market consumers in 37 states. Z-Tel offers its services by means of unbundled network elements, a key method of entry provided for by Section 251(c)(3) of the Communications Act of 1934, as amended. Z-Tel is intensely interested in the outcome of this proceeding because a fully-functioning competitive market, especially for the mass-market

consumers of analog services that Z-Tel seeks to serve, depends upon orderly transfer of customers and assets between ILECs and CLECs and CLECs and CLECs, regardless as to whether one party is or is not in bankruptcy.

In these Comments, Z-Tel takes no position as to whether IDT Winstar assumed or rejected any executory contracts in its pending bankruptcy proceeding. However, in the context of this dispute, Verizon has specifically asked the Commission to determine rights and obligations under the Communications Act that stand contrary to the *Buntner* principle. In its zeal to slash and burn the remaining assets of Winstar, Verizon has proposed that the Commission countenance incumbent LEC insistence of full payment and establish special obligations upon competitors that have filed for bankruptcy. Those proposals should be soundly rejected.

As discussed below, Verizon, like other incumbent LECs, is far from an ordinary "creditor" – it is, in fact, a dominant provider of bottleneck local facilities that competitors like Winstar must do business with in order to be a viable telecom provider. While CLECs often have some choice in they types of commercial debt they issue and holders of bank debt, CLECs most assuredly *do not* have a choice in whether to do business with an incumbent LEC like Verizon. Compounding this situation is the fact that this necessary creditor – the ILEC – is *also a competitor* of the debtor CLEC, and indeed may be the CLEC's principal competitor. Unlike other creditors, who have in interest in maximizing the value of the debtor CLEC and perhaps even maintaining the viability of the debtor CLEC as an ongoing concern, the competitor-creditor ILEC has no such interest. In fact, it may be in the long-term business interest of the competitor-creditor ILEC's interest to drive the debtor CLEC out of business and liquidate its assets in as "messy" a process as possible, so as to stamp out all future hope of competition.

In considering Verizon's Petition, the Commission must take these divergent ILEC interests into account. More importantly, bankruptcy may be the point when a CLEC, its customers and creditors are *most* dependent upon the incumbent LEC, especially if that incumbent LEC is threatening to disconnect services. As a result, the Commission must vigilantly enforce incumbent LEC obligations to provide service in such circumstances and ensure an orderly and seamless transition of the customer base if a CLEC emerges from bankruptcy. Instead, Verizon asks the Commission to help it jump in front of other unsecured creditors, for no apparent public interest justification. For the Commission, the needs are affected customers and ensuring nondiscriminatory incumbent LEC wholesale service provision must be paramount – the Commission should not abuse its authority to become a collection agent for incumbent LECs.

I. INCUMBENT LECS ARE NOT "ORDINARY" CREDITORS

An overarching theme of Verizon's Petition (and BOC comments in this proceeding) is that they are entitled to their ordinary rights under the Bankruptcy Code to receive full payment for assumed or assigned executory contracts. These arguments fail to recognize that incumbent LECs *are* different than "ordinary" debtholders or parties to executory contracts – because they are incumbent LEC monopolists that the Communications Act imposes special duties upon. The Commission would be remiss to address the Verizon Petition without addressing this fundamental fact.

Incumbent LECs hold incredible power over the value of all CLEC enterprises. Because incumbent LECs control access to bottleneck facilities, *any* CLEC that wishes to offer local service *must* have an interconnection agreement with the incumbent LEC or purchase services through an incumbent LEC tariff. And if the value of a CLEC enterprise includes acquired

customer base and operations, to maintain the value of that enterprise during bankruptcy, a CLEC will need to maintain a post-petition relationship with that incumbent LEC.

At the same time the CLEC is doing business with an incumbent LEC, that incumbent LEC is a *competitor* of the CLEC. A creditor that is a bank or equipment vendor have a direct, pecuniary interest in seeing the CLEC succeed – but the competitor-creditor incumbent LEC has the quite opposite interest. As a result, it may be in the interests of the incumbent LEC to force liquidation of the complete debtor CLEC enterprise, rather than accept a reorganization that continues the CLEC as a viable commercial enterprise. An incumbent LEC also has a *very strong* incentive to scuttle the transfer of customers from a bankrupt CLEC to a more financially-stable competitor. What company would want to help form a financially-stable competitor?[1]

Because the competitor-creditor incumbent LEC has market power over bottleneck local facilities, it is in the unique position to cause liquidation or block transfer of customers to a financially-secure CLEC. The Commission certainly should not assist in this effort. Instead, it is at this point in the process that enforcement of the Communications Act is most critical. Under the Act, incumbent LECs owe certain specific, statutory duties to requesting carriers, and the Commission has the duty to enforce those obligations and also the public mandate to ensure minimal service disruption for consumers.

In short, Commission policies developed in response to this proceeding or Verizon's petition must take into account the fact that the competitor-creditor incumbent LEC has interests

[1] Indeed, management of incumbent LECs may have a fiduciary duty under corporation law principles to resist any such result. Should the Commission temper incumbent LEC duties under Section 251 to render them harmonious with the fiduciary duty of incumbent LEC management to maximize their shareholder value? How is this proceeding any different?

very different than ordinary creditors like banks and bondholders.[2] An incumbent LEC can quickly torpedo a CLEC enterprise in bankruptcy by taking actions such as disconnecting customers, resisting the swift transfer of customers to acquiring companies, and insisting on full payment.

In this time of severe customer uncertainty, there is also an important interest in ensuring that legal bodies "stick to their knitting." The Commission is obligated to protect this public interest and put in place policies that promote the swift and painless transfer of customers from one carrier to another in circumstances such as bankruptcy. The Commission should enforce the common carrier obligations of incumbent LEC monopolists like Verizon and not permit incumbent LEC monopolists to threaten bankrupt CLECs and ordinary creditors with disconnection of service if full payment is not received.

II. VERIZON'S PROPOSAL THAT THE COMMISSION IMPLEMENT SPECIAL NOTICE RULES FOR BANKRUPT CLECS SHOULD BE REJECTED

Verizon asks that the Commission write special customer "notice" rules for CLEC customers when a CLEC declares bankruptcy.[3] While Z-Tel takes no position as to whether IDT Winstar has fully complied with the Commission's service disconnection rules and policies, the Commission should not put in place a special set of notice rules for CLECs that declare bankruptcy. Verizon's proposal is nothing more than a transparent attempt to scare CLEC customers and to turn bankruptcy proceedings into retail "win-back" opportunities.

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2 Indeed, Verizon recognizes these divergent interests, noting that if it receives full payment, such action "reduce[s] the amounts paid to other creditors." Verizon Commentat and Petition at 22.

3 Verizon Comments and Petition at 20 ("When a carrier files in Chapter 11 and initiates an auction of its assets, the carrier should certainly have to inform customers of a possible discontinuation of service."), 26.

A fundamental principle of bankruptcy law is that the legal and property rights of a bankrupt person should not be treated differently solely because that person is involved in bankruptcy. *See Butner v. United States*, 440 U.S. 48 (1979). According to noted commentators, to treat the non-bankruptcy legal rights of persons differently once they declare bankruptcy "would invite people to seek or avoid the bankruptcy forum for reasons that had nothing to do with the policies bankruptcy law advances."[4] Requiring CLECs to provide special notice to customers about the potential for disconnection when a bankruptcy petition is filed would create unnecessary customer confusion, would materially diminish the value of the CLEC customer-base asset, and would discourage CLECs from taking advantages of the protections accorded by the Bankruptcy Code.

The Commission should recognize that such special notice rules would have the obvious effect of encouraging customers to voluntarily leaving the bankrupt CLEC. Aside from providing the incumbent LEC with a nifty retail "win-back" opportunity, special notice requirements would have the expected effect of diminishing the value of the CLEC's customer base asset. The fact that Verizon, an incumbent LEC creditor would favor such an action that other creditors would no doubt oppose demonstrates clearly that incumbent LEC competitor-creditors have widely divergent interests than ordinary unsecured creditors in a bankruptcy proceeding, as discussed above.

Other than the instant IDT Winstar dispute, Verizon provides no evidence that the Commisison's current service disconnection and notice rules have failed to protect the public in the spate of other CLEC bankruptcies that have closed or are pending. Without such a record,

[4] Douglas G. Baird, Thomas H. Jackson, Barry E. Adler, *Bankruptcy* (2000) at 29.

the Commission has no basis for determining that special notice rules for CLECs in bankruptcy are needed.

III. VERIZON'S INSISTENCE ON FULL PAYMENT IS CONTRARY TO THE PUBLIC INTEREST

Verizon also asks that the Commission rule that when a CLEC "take[s] over another's service arrangement with nothing more than a name change", the assignee "must assume the outstanding indebtedness of the prior CLEC for such services."[5] It is also apparent that Verizon seeks to enforce its claim for full payment of all pre- and post-petition debt by threatening to disconnect service.

Verizon wants the Commission to put in place a rule of law that would allow incumbent LECs to jump ahead of all other creditors and be assured of *full payment* for all pre- and post-petition debt. That result is directly contrary to the purpose of the Bankruptcy Code and advances no public policy mandated by the Communications Act. That result also fails to recognize that incumbent LECs have market power and have an incentive to destroy the value of a CLEC enterprise rather than see the customer base of the debtor CLEC enterprise end up in the hands of a more financially-secure competitor. Verizon's request should be soundly rejected.

Verizon provides *no public policy justification* for this Commission action other than the fact that its tariffs contain language that Verizon construes in its favor. Verizon provides no rationale for its belief that it – the incumbent LEC – must be paid in full, even to the extent of potentially scuttling the entire debtor CLEC business, while customers and other creditors are left holding the bag.

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[5] Verizon Petition at 26. The Commission should make clear Verizon's Petition can only extend to Verizon's federal tariffs and can have no legal impact upon CLEC obligations in interconnection agreements or under state tariffs. Those legal obligations are for courts and state commissions to decide.

The Winstar dispute is not the only context in which a BOC – particularly Verizon – engaged in anticompetitive strategies designed to thwart transition of customers or assets to more financially-stable competitors. The Comments of Cavalier Telephone in this proceeding describe anticompetitive conduct by Verizon when Cavalier acquired Net2000 customers. In addition, last year Z-Tel sought to acquire from a now-defunct CLEC a Class V switch and 39 Verizon collocation arrangements in New York City to service customers that Z-Tel was serving by means of the unbundled network element platform. Despite Verizon's stated position in favor of transitioning carriers from UNE Platform to switch-based entry, Verizon insisted on full payment of $4 million by Z-Tel to make up for the back-payments Verizon believed it was owed by the now-defunct CLEC. Verizon's insistence of full payment – combined with the inability to transition sufficient number of customers in sufficient quantity and quality and other factors – forced Z-Tel to abandon this effort to acquire a switch.

The Commission must be mindful that the competitor-creditor incumbent LEC has an interest that differs radically from the interests of the debtor CLEC, customers, other creditors, and potential acquirers like Cavalier and Z-Tel. While the customers and creditors of the debtor CLEC may be far better off in the event a willing and financially-stable purchaser is found for the debtor CLEC customer base or assets, the competitor-creditor incumbent LEC has little, if any, interest in seeing that transaction consummated. The Commission should expect incumbent LECs to seek to prevent such transactions from happening by putting in roadblocks to such transitions, as Verizon did with Cavalier and Z-Tel.

The Commission's interest in this situation should be to ensure continuance of service to customers and the swift and painless transfer of customer bases and assets to other carriers if that is the route the bankruptcy court approves. The Commission should not require carriers seeking

to acquire CLEC customers out of bankruptcy or other means to "disconnect" and then place new "reconnect" orders, which run the risk of being denied on account of lack of facilities.

Z-Tel agrees with Winstar that implementing this "disconnect/reconnect" policy in incumbent LEC tariffs is unreasonable under Sections 201, 202 and 251 of the Act.[6] Incumbent LECs are dominant carriers, and the imposition of unnecessary costs by dominant carriers are unreasonable practices.[7] Z-Tel also agrees that adjudicating the terms of Verizon's and other BOC tariffs on this point are well beyond the scope of this proceeding. That said, the fact that BOCs have not always followed the provisions of these "full payment" tariff clauses renders their terms unlawful, especially because selective enforcement of a tariff provision by an incumbent LEC gives rise to significant public policy concerns.

In this time of severe financial distress for the CLEC industry, the overriding public policy concern should be that end-users not experience unnecessary dislocation or interruption of service. One of the major assets of a CLEC may be its customer base, and permitting an incumbent LEC to hold that asset hostage while the CLEC is in bankruptcy would be contrary to public policy. To the extent the Commission inserts itself into this process, the Commission should establish policies that encourage and facilitate the transfer of customers and assets from CLECs to other carriers. In setting the policies, the Commission must be mindful that incumbent LECs, unlike other creditors and customers, should be expected to resist such transfers to financially-secure competitors.

IV. CONCLUSION

The Commission cannot allow itself to become a collection agent for incumbent LECs, yet this is precisely what Verizon and other BOC commenters want. Incumbent LECs are not

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[6] Winstar Reply at 12.

ordinary creditors of CLECs – they are competitors that possess market power that CLECs *must* do business with in order to be in business. As such, unlike other creditors and potential acquirers, incumbent LECs have an incentive to interfere with, and not facilitate, the seamless transfer of customers and assets from one CLEC to another.

The Commission must reject the BOC pleas for it to adjudicate their rights in bankruptcy and instead should protect the public interest by ensuring that CLEC customer transfers happen as seamlessly and efficiently as possible. Incumbent LECs should be prohibited from putting roadblocks in the way of such transitions – either through disconnect/reconnect artifices or through insisting on full payment while a CLEC is in bankruptcy. As a result, Verizon's Petition in this proceeding should be rejected.

Respectfully submitted

S/[filed electronically]

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[7] Winstar Reply at n.27.